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IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

LEONARD NOBELMAN and HARRIET NOBELMAN,

Petitioners,

vs.

AMERICAN SAVINGS BANK,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

BRIEF FOR AMICI CURIAE FEDERAL HOME LOAN MORTGAGE CORPORATION AND MORTGAGE BANKERS ASSOCIATION OF AMERICA IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED FOR REVIEW

Does Section 1322(b)(2) of the United States Bankruptcy Code, 11 U.S.C. §§ 101-1330 (the "Bankruptcy Code"), which provides special protection for residential mortgage lenders in cases under Chapter 13 of the Bankruptcy Code, prohibit a Chapter 13 debtor from modifying the rights of a creditor holding a claim secured only by a mortgage on debtor's principal residence by "cramming down" that creditor's claim to the value of the

property under Section 506(a) of the Bankruptcy Code, and then discharging the balance of the claim with unsecured debts under a Chapter 13 plan?

Amici Curiae Federal Home Loan Mortgage Corporation ("Freddie Mac") and Mortgage Bankers Association of America ("MBAA") agree with Petitioners that the Court should grant the petition for a writ of certiorari in this case in order to resolve this important issue.

STATEMENT OF INTEREST OF AMICI CURIAE

Freddie Mac is a corporate instrumentality of the United States, chartered by Congress as part of the Emergency Home Finance Act of 1970, Pub. L. No. 91-351, tit. III, 84 Stat. 450 (codified as amended at 12 U.S.C. §§ 1451-59). Its statutory mission is to foster and promote a secondary market for the purchase and sale of mortgages on residential property.

Freddie Mac acts in the secondary mortgage market to increase the liquidity of mortgage investments and thereby make more capital available for home financing. Banks, savings associations and other lenders originate loans in the primary mortgage market, and then sell those loans in the secondary mortgage market to Freddie Mac. Freddie Mac, in turn, resells the mortgages to investors in the form of mortgage pass-through securities which represent interests in groups of mortgages. With the funds received from the resale of the mortgages, Freddie Mac purchases more mortgages from originating lenders who in turn make those funds available to home purchasers. The secondary mortgage market thus greatly increases the supply, and reduces the cost, of home mortgage credit to America's homeowners.

The smooth functioning of this market depends upon a predictable flow of principal and interest from home mortgages. Where cram-down is permitted, and borrowers are allowed unilaterally to reduce the balance of their mortgage loans, this predictability is undermined. Freddie Mac and other entities operating in the secondary mortgage market therefore have a strong interest in the resolution of the question presented for review in this case.

MBAA is a non-profit corporation headquartered in Washington, D.C. and existing under the General Not For Profit Corporation Act of Illinois. MBAA is the primary national trade association devoted exclusively to the field of mortgage and real estate financing. Mortgage banking firms, which comprise the largest part of MBAA's total membership of 2600 corporations, engage directly in originating, financing, selling and servicing mortgages. "Origination" is the bringing of the mortgage into existence as the result of negotiating, arranging, and funding the loan to home buyers. "Servicing" is the collection of payments on existing loans, monitoring the payment of real property taxes and other charges to protect the priority of the mortgage lien, and facilitating the realization of the security in the event of nonpayment. In 1991, mortgage bankers originated more than $298 billion in single-family mortgages and serviced in excess of $1 trillion in single-family mortgages. Especially significant in the context of this case, MBAA members originate and service 65 to 80 percent of the home purchase mortgages in programs that Congress has designed to encourage home ownership by facilitating low down payment loans to home buyers.

SUMMARY OF ARGUMENT

The Court should grant the petition for a writ of certiorari. The question of whether the special protection afforded to residential mortgage lenders under Section 1322(b)(2) of the Bankruptcy Code protects those lenders from "cram-down"– that is, forced reduction of the amount of the loan in question to the value of the collateral securing it – is one of national scope and considerable importance, both to institutions such as MBAA and Freddie Mac, which operate in the primary and secondary mortgage markets, and to American homeowners, whose ability to obtain mortgage credit will be affected if "cram-down" is permitted. In holding that "cram-down" is not permissible under Section 1322(b)(2) of the Bankruptcy Code, the Fifth Circuit Court of Appeals is in direct conflict with four other circuit courts of appeals on the question presented. Clear resolution of the permissibility, or lack thereof, of cram-down is necessary to avoid complete uncertainty in the primary and secondary

mortgage markets. Further, different rules in different circuits would result in certain loans being available to potential homebuyers but not to others based solely upon the state in which they happen to reside.

ARGUMENT FOR GRANTING WRIT OF CERTIORARI

1. The Circuit Courts of Appeals Have Rendered Conflicting Decisions Regarding the Ability of a Chapter 13 Debtor to Cram-Down a Residential Mortgagee's Claim

The Court of Appeals for the Fifth Circuit has held that Section 1322(b)(2) of the Bankruptcy Code precludes Chapter 13 debtors from "cramming down" the secured claim of a mortgagee holding a lien on the debtor's principal residence to the value of the property. *Nobelman v. American Savings Bank*, 968 F.2d 483 (5th Cir. 1992). Four other circuit courts addressing this question have issued decisions that directly conflict with the Fifth Circuit's decision. Those courts have permitted "cram-down" of a residential mortgage holder's claim notwithstanding the special protection afforded to such a creditor by Section 1322(b)(2) of the Bankruptcy Code. *See Bellamy v. Federal Home Loan Mortgage Corporation*, 962 F.2d 176 (2d Cir. 1992); *In re Hart*, 923 F.2d 1410 (10th Cir. 1991); *Wilson v. Commonwealth Mortgage Corp.*, 895 F.2d 123 (3d Cir. 1990); *In re Hougland*, 886 F.2d 1182 (9th Cir. 1989).

Three of the decisions allowing cram-down by Chapter 13 debtors were decided prior to the decision in *Dewsnup v. Timm* ___ U.S. ___, 112 S. Ct. 773 (1992), in which this Court held that a Chapter 7 debtor may not "cram-down" a creditor's lien on real property to the value of the collateral when that value is less than the amount of the claim secured by the lien. Although the fourth case, *Bellamy*, was decided after *Dewsnup*, all briefs were submitted and oral argument completed before the *Dewsnup* decision was rendered. Thus, Freddie Mac and amici curiae (which included MBAA) in that case did not have the opportunity to explain the full impact of the *Dewsnup* decision

to the Second Circuit.* Indeed, at least one court, in addition to the Fifth Circuit, has held that the decisions allowing cram-down of a residential mortgage holder's claim in Chapter 13 cases had been "weakened, if not demolished, by *Dewsnup*". *In re Strober*, 136 B.R. 614, 618 (Bankr. E.D.N.Y. 1992).

In addition, the decisions of the Third, Ninth and Tenth Circuits permitting cram-down were rendered without the benefit of briefing by Freddie Mac or MBAA, or any similarly situated *amici curiae*. As a result, in making their decisions those courts did not have the opportunity to consider such matters as the negative impact that a decision allowing "cram-down" of residential mortgage debts could have on the primary and secondary mortgage markets, or the impact of such a decision on the Congressional policy favoring investment in home ownership that was the basis for Section 1322(b)(2) of the Bankruptcy Code.

2. The Resolution of This Issue Will Have an Important Impact on the Secondary Mortgage Market and on Availability of Credit to Potential Homebuyers

It is important that this Court grant certiorari in this matter because resolution of the question of whether Chapter 13 debtors may "cram-down" their home mortgage lender could have a significant impact on the secondary mortgage market and on the availability of credit for home purchases generally.

The secondary mortgage market, in which Freddie Mac operates, may be impaired if Chapter 13 debtors are permitted to cram-down the claims of residential mortgagees. In the secondary market, banks, savings associations and other lenders sell mortgages to Freddie Mac and other institutions which in turn, resell the mortgages in the form of mortgage-backed securities. This process, fostered by substantial Congressional

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* Freddie Mac petitioned the Second Circuit for rehearing and rehearing *en banc* based, in part, on the *Dewsnup* decision. The Second Circuit, however, denied the request for rehearing.

legislation, has greatly increased the availability of home mortgage credit in the United States.

However, the secondary mortgage market only can offer such advantages to the individual home buyer if a predictable flow of principal and interest from mortgages can be maintained. If cram-down is permitted, and borrowers are allowed unilaterally to reduce the balance of their mortgage loans, this predictability is undermined, and the ability of entities operating in the secondary mortgage market to continue to supply low-cost and plentiful credit to America's homeowners may be adversely affected.

The resolution of this issue is all the more important because of the skyrocketing numbers of personal bankruptcy filings. According to a recent article in the Washington Post, personal bankruptcies have reached record levels over the past seven years, more than tripling since 1984. In 1991, 872,000 people filed for personal bankruptcy, 150,000 more than in 1990, which is by far the largest increase in a single year. *See* Carolyn Hughes Crowley, *You; Bankrupt; No Way Out; Many Americans Can't Even Afford to File*, Washington Post, May 5, 1992 at B5. Indeed, a record 252,733 personal bankruptcies were filed during the first quarter of 1992. *See Short Cuts*, Newsday, October 6, 1992, Business Section at p. 31.

While a portion of those personal bankruptcies are Chapter 7 cases, Chapter 13 is becoming increasingly popular and the number of these cases have similarly exploded. According to statistics compiled by the Administrative Office of the United States Courts, 244,192 Chapter 13 cases were filed for the year ended June 30, 1991. *Report on the Judicial Conference, Report of the Administrative Office of U.S. Courts* 1991 at p297. For the following year, ended June 30, 1992, 267,121 Chapter 13 cases were commenced – an increase of over 9%. *Statistical Tables for Twelve Month Period Ended June 1992.*

With the continually increasing rise in the number of Chapter 13 filings, the need for a clear resolution of the availability of cram-down is all the more urgent. Freddie Mac and MBAA therefore respectfully submit that the petition for writ of certiorari in this case should be granted.

CONCLUSION

The petition for writ of certiorari should be granted.

November 11, 1992

Respectfully submitted,

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